

Testimony of
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Board of Directors

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My name is Jack W. Simmons. I serve as the President and CEO of the Tennessee Valley Public Power Association, Inc., (TVPPA), based in Chattanooga, Tennessee.

TVPPA is the nonprofit, regional service organization representing the interests of the 158 municipal and cooperative electric utilities who purchase wholesale electric power from TVA. TVPPA serves as an advocate of its members' interests with the public, in the political process, and with TVA.

The purpose of my testimony today is to provide background information to the TVA Board of Directors on the issue of transmission access for the distributors of TVA power, and to describe to the TVA Board the collaborative efforts that have taken place among various stakeholder parties to resolve differences in positions on this very complicated and sensitive issue.

Policies set forth by the TVA Board of Directors as a result of the information gathered during this hearing and from other sources used in the Board's due diligence process, will have historic consequences, and will provide a new platform for the future relationship among TVA and the power distributors in the Tennessee Valley.

TVPPA recognizes the serious nature of these deliberations, and offers its perspective and a potential contractual framework that identifies and addresses the common interests, rather than the positions, among various stakeholder groups.

TVA and TVPPA have been discussing the issue of transmission access for many years. In fact, it was a joint effort by both parties to influence the shaping of the Energy Policy Act of 1992 (EPA92), to include a provision to protect TVA and the distributor community in the Tennessee Valley from the almost certain cherry-picking of TVA distributors by other wholesale power providers outside the TVA service territory. TVPPA and TVA jointly and actively supported legislation that included an anti-cherry picking amendment. The legislation resulted in a

new Section 212(j) in the Federal Power Act, which provides that FERC cannot require TVA to provide transmission service to other parties to serve distributors inside the TVA service territory. It is our interpretation that while Section 212(j) does not require TVA to provide transmission service into the Valley; it also does not prohibit TVA from allowing such transmission service to occur. Therefore, we believe TVA can unilaterally allow distributors to use the TVA transmission system for the delivery of power from sources outside the Valley, after exercising appropriate cancellation rights under their power contracts with TVA. Consequently, additional legislation is not required to allow distributors to receive transmission service for alternative power supplies. As a result of the anti-cherry picking amendment, TVA and distributors in the Valley have been insulated and protected from many of the mistakes and misfortunes that occurred across the country following wholesale deregulation. However, distributors were also prohibited from experiencing some of the benefits of deregulation.

As wholesale deregulation matured across the country following EPA92, concerns arose among TVA, Distributors, and TVA's direct-served customers, that future deregulation efforts could potentially have harmful impacts on the TVA region. As a result, the parties jointly developed and agreed to language commonly referred to as the TVPPA/TVA/TVIC Consensus Title. The Title was a defensive mechanism to be used as preferred legislative language in case alternative legislation affecting the Valley was proposed by others. The Consensus Title language included, among other provisions, that Section 212(j) be repealed, allowing transmission into the Tennessee Valley Region, and further, that the TVA Act be revised to allow TVA to sell power outside the area to which TVA was limited in the 1959 Amendment to the TVA Act. In other words, the fence was to be taken down in BOTH directions. The Consensus Title has never been adopted in any legislation, but the TVPPA membership and the TVA Board have both committed to support such language if appropriate conditions develop in any proposed legislation that would trigger the need for such language.

In short, even though both TVA and TVPPA supported putting UP the fence into TVA in 1992, both parties supported taking DOWN the fence in BOTH directions as part of the Consensus Title in the mid-1990's.

In 1997, TVA encouraged distributors to enter into new 10-year power supply contracts that allowed a five-year notice, after the first five years, to remove their entire load from the TVA system, i.e., a 5 + 5 contract. These new contracts also provided that after the 10-year period (2007), there would be no claim by TVA of any stranded costs associated with the contract cancellation. Currently, six of the 158 distributors in the Valley have exercised the notice provisions of the 1997 contract, and plan to purchase power from suppliers other than TVA. Three additional distributors gave notice, and have since rescinded such notice. They currently remain with TVA as their power supplier. For those distributors who

have given notice, TVA has taken the position that the notice provision applies only to the supply of power and energy from the TVA power system, and does not include transmission service to support power and energy delivered by a non-TVA generating source. As a result, these six distributors are facing difficulties in exercising their choice of alternative power suppliers. Without transmission service from TVA, several of these distributors are faced with substantial capital expenditures for new transmission and/or interconnection facilities.

In an effort to require TVA to provide such transmission service, noticing distributors have appealed to the political process for new provisions in Federal law that would exempt certain distributors from the anti-cherry picking amendment and Section 212(j) of the Federal Power Act. TVPPA has strongly opposed such legislation because it does not provide similar provisions for ALL distributors in the Valley. The TVPPA Board of Directors has been firm in its convictions that it will not interfere with contractual or legislative rights of any individual member system, but that if any system is to receive new contractual or legislative rights, then ALL TVPPA member systems should receive the same rights. As a result, TVPPA met with key Congressional offices, in cooperation with TVA, to explore ways to avoid legislative action that is inconsistent among distributors. A clear message was received from five key Senate offices that a non-legislative, contractual solution would be a preferred vehicle for all parties involved.

TVPPA has developed a non-legislative framework that, we believe, addresses the interests of all stakeholders in a fair and equitable manner. A draft copy of the framework document is attached to this testimony. It represents the collaborative work of the TVPPA Steering Committee, and is proposed to be the framework for negotiations with TVA executive management.

TVPPA has been in collaboration with distributors, key TVA staff, the previous full-time executive TVA Board, and Congressional staff throughout the process of developing this framework. In spite of the acceptance of the TVPPA framework by distributors of all types (current noticing distributors, future noticing distributors, and non-noticing distributors), the previous TVA Board felt uneasy in adopting the TVPPA framework as a basis for continued negotiations. They suggested that the new part-time policy Board of TVA should have an adequate chance for review and input from all parties, prior to adopting a policy. TVPPA believes this is a reasonable position, and is committed to providing the new TVA Board with as much information as needed for a clear understanding of the TVPPA framework and the TVPPA approach to resolving the issues related to transmission access.

The following five principles have been embraced by TVPPA in developing the framework document.

1. TVPPA supports the principle that a contractual arrangement for partial requirements and transmission access can be developed, that allows distributors to explore alternative power supply options.
 - a. Partial requirements contracts would enable distributors to purchase some or all of their power from alternative suppliers, and/or to purchase, construct, and own their own generation and transmission assets.
 - b. Transmission access would be provided to distributors by TVA on a comparable, just and reasonable, and non-discriminatory basis to accommodate partial requirements contracts.
2. TVPPA supports the principle that such arrangements must meet the needs of all distributors, including those who have already given notice, those who may give notice in the future, and those who currently have no desire to give notice.
3. TVPPA supports the principle that such arrangements would allow TVA to operate on a fiscally sound basis, and would mitigate undue cost shifting among distributors and other TVA customers.
4. TVPPA supports the principle that the TVA Fence should be modified by legislation to allow TVA the ability to sell, on a pro-rata basis, power to counterparties beyond those 14 identified in the 1959 amendment to the TVA Act. TVPPA pledges its support to TVA and to the Valley Congressional delegation to pass such legislation as soon as practicable.
 - a. However, TVPPA believes that such a legislative change is not a prerequisite to accommodating partial requirements and transmission access. Instead, a measured and managed approach can be used to mitigate impacts to TVA, distributors and other customers
 - b. The principle of a ratable departure level, i.e., allowing a measured, incremental amount of distributor load to leave the TVA system annually, would allow TVA and distributors to manage and mitigate the effects of lost load on TVA and on those distributors who choose not to leave.
5. TVPPA supports the principle that there should be offsetting benefits to those distributors who have not given notice, in order to allow those six

distributors who leave under their current contract notice provisions to receive the immediate benefits of transmission access for their entire load.

- a. The six distributors who have given notice must:
 - Remove their entire load from the TVA system at the time of contract expiration.
 - Relinquish all other non-transmission related services and benefits.
 - Relinquish all preference rights to the output of current and future TVA generation assets.
 - Suffer no stranded cost recovery from TVA.
 - Consider good faith offers from TVA of short-term quantities of power and energy to mitigate any impacts of fixed-cost shifting to non-noticing distributors and other TVA customers.
- b. Distributors who have not given notice may:
 - Give notice in the future under the ratable departure levels.
 - Implement partial requirements contracts.
 - Retain all other non-transmission related services as long as their partial requirements contract remains above a threshold level.
 - Retain all preference rights to the output of current and future TVA generation assets for that amount of load and load growth that remains with TVA.
 - Suffer no stranded cost recovery from TVA.
 - Participate in distributor-owned generation arrangements with TVA.
- c. The six distributors who have given notice may reconsider their current notice provisions, without consequence or increased costs, in order to receive the same benefits, terms, and conditions developed for distributors who have not given notice.

TVPPA is committed to negotiate in good faith with TVA executives to develop and implement contractual arrangements that embrace these principles. TVPPA has coordinated these principles and the proposed framework for implementation with distributors who have already given notice, those who may give notice in the future, and those who currently have no desire to give notice. TVPPA has also coordinated these principles and the proposed framework for implementation with key staff in the offices of Sens. Frist, Alexander, Bunning, Cochran, and McConnell.

TVPPA makes the following requests and commitments to the TVA Board of Directors:

1. TVPPA requests that the TVA Board of Directors embrace the principles of TVPPA's proposed framework for partial requirements and transmission access using a measured and managed approach.
2. TVPPA requests that the TVA Board of Directors provide policy guidance, embracing such principles, to its Acting Chief Executive Officer, delegating the authority to proceed in the development of a detailed term-sheet and contractual arrangement that implements these principles.
3. TVPPA commits to actively support timely legislation for a pro-rata fence modification. At the time of such legislation, TVPPA suggests that the ratable departure level be reevaluated and modified as appropriate to reflect the decreased risk of loss of distributor load.

In conclusion, TVPPA has earnestly attempted to separate the positions from the interests of the parties involved in this very important debate. It has become obvious during the evolution this framework that the common underlying interest is that of a reliable, cost-effective power supply for the consumers in the Tennessee Valley. The desire by some to give notice to cancel the TVA power contract is driven by this same interest. We believe it is in the best long-term interest of the Tennessee Valley to craft strategies and solutions that maintain the integrated public power model in the Tennessee Valley. By understanding the needs and the interests of all involved, and by developing compromise solutions to meet the majority of those needs, we can continue the legacy of those who conceived this great experiment 73 years ago today.

Thank you for allowing me to participate in this historic occasion.

This is a deliberative pre-decisional DRAFT document of TVPPA. It represents the collaborative work of the TVPPA Steering Committee, and is proposed to be a Framework for negotiations with TVA executive management.

DRAFT – May 18, 2006

**Essential Elements of a Comprehensive Non-Legislative Plan
for Partial Requirements, Transmission Access, and Asset Ownership¹**

- a. Immediate transmission access waiver for current noticing distributors (with the following conditions)
- b. Current and future noticing distributors receive just and reasonable, non-discriminatory transmission access at FERC proforma tariff rates, terms, and conditions.² Transmission service and/or interconnection with coordination services to be available to current and future noticing distributors at the end of the cancelled contract term. Transmission service arrangements may include Network Integration Transmission Service, Firm Point to Point Transmission Service, and other types of transmission services, including Ancillary Services, identified in TVA's Transmission Service Guidelines.
- c. Current and future noticing distributors relinquish non-transmission related programmatic services and benefits, such as economic development and energy services programs, effective at time of formal notice of contract cancellation.
- d. Current and future noticing distributors relinquish all preference rights to output of TVA's current heritage generation assets and future TVA generation assets at the time of formal notice of contract cancellation, but continue to receive power and energy at prevailing system average rates for the remainder of the cancelled contract term.
- e. Following the expiration of the cancelled contract term, current and future noticing distributors relinquish rights to future surplus power from TVA heritage generating assets for the portion of their load removed from the TVA system, but by mutual agreement, may purchase power

¹ Three classes of distributors are referenced

- Current noticing distributors
- Future Noticing distributors (includes future partial requirements distributors)
- Non-noticing distributors

² TVA shall provide transmission service at rates, terms and conditions that are just and reasonable and not unduly discriminatory or preferential, in keeping with the requirements and standards of sections 205, 206 and 211 of the Federal Power Act. If the parties are unable to agree on the rates, terms and conditions of transmission service, FERC will resolve the disputes pursuant to section 211 of the Federal Power Act, unless the parties mutually agree to an alternative procedure for binding dispute resolution (i.e., TVA will not assert that FERC lacks jurisdiction under section 211 to resolve disputes).

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and energy from the TVA system at negotiated market-based prices, terms, and conditions.

- f. Current noticing distributors cancel their entire full-requirements power supply contract with TVA. Future noticing distributors retain the option to cancel only a portion of their TVA contract (partial requirements).
- g. Current noticing distributors have a one-time grace period (180 days) to reconsider, without consequence or increased costs, the withdrawal of their current contract cancellation notice in order to receive the same benefits, terms and conditions developed for future noticing or non-noticing distributors. Future noticing distributors receive no grace period once formal contract cancellation notice has been given for any portion of their contract.
- h. TVA will not seek to recover stranded costs from any noticing distributor. However, at the end of the cancelled contract notice period, current and future noticing distributors will seriously consider good-faith offers from TVA of short-term quantities of power and energy at negotiated rates for a portion of the load removed from the TVA supply plan (to mitigate impacts of fixed-cost shifting to non-noticing distributors).
- i. Non-noticing distributors retain exclusive rights to continued forward purchase of output of TVA's current heritage generation assets and future TVA generation assets.
- j. Future noticing distributors have the right to cancel a portion (0% to 100%) of their TVA contract (partial requirements), under similar conditions and with similar rights for the cancelled load, as current noticing distributors, subject to ratable departure levels.³
- k. Partial requirements to include options for distributor self-generation or purchase from a supplier other than TVA.
- l. TVA and non-noticing distributors will develop arrangements for distributor ownership/financing for a portion of TVA's current heritage generation assets and future TVA generation assets.

³ Ratable departure levels to be developed and described that allow future noticing distributors to implement partial requirements power supply arrangements. Annual ratable departure level to be adequate to allow reasonable and sufficient optionality for multiple distributors to evaluate and implement partial requirements options, yet limited to the extent that undue cost shifting among distributors is mitigated, and adverse ratings of TVA bonds are minimized. Current noticing distributors would be allowed to remove the entire amount of their load at the time of their contract term expiration.

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- m. Formal TVPPA Board Resolution and signed commitment by current noticing distributors to actively support timely legislation for a pro rata fence modification.⁴
- n. Formal TVA Board Resolution supporting the elements described herein.
- o. In the event that timely legislation for a pro rata fence modification cannot be effectively implemented, the foregoing arrangements will be implemented with a lower initial ratable departure level, until legislation for a pro rata fence modification is implemented, at which time the ratable departure level will be reevaluated to reflect TVA's legislated ability to sell wholesale power outside the current fence.
- p. The effective date for the transmission access waiver for any current noticing distributors would be at the expiration of their respective contract cancellation period.
- q. The effective date for transmission access and partial requirements for any future noticing distributor would be at the expiration of any future contract cancellation period, with the amount of partial requirements limited by the available amount of energy determined by the cumulative ratable departure level (MWh).
- r. In addition to the above specific items, TVPPA and TVA will continue in good faith discussions and negotiations to develop a contract for an improved long-term relationship between TVA and the distributors that addresses the following specific issues.
 - i. Contract term length – new contract form for all distributors that allows status quo if desired
 - 1. Layered contracts (multiple term lengths)
 - 2. Adequate coverage for hedging asset financing
 - ii. Pricing methodology for multiple term lengths
 - iii. Credits for debt reduction
 - iv. Appropriate disposition of Consensus Title issues
 - v. Modified rate change and rate adjustment process, including a Fuel Cost Adjustment Mechanism with distributor oversight
 - vi. Preservation of Public Power (cost-based) principles in pricing of products and development of ownership models

⁴ Pro rata fence modification means TVA would have the ability to enter into wholesale power exchange arrangements with any wholesale entity, in addition to those identified in the 1959 amendment to the TVA Act, equivalent to the amount of energy (MWh) removed by a current or future noticing distributor from the TVA system, i.e., the amount to be served by a wholesale power supplier other than TVA. The amount of energy to be removed by a future noticing distributor would be limited by the available amount of energy determined by a cumulative ratable departure level.

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DRAFT – May 18, 2006

**Essential Elements of a Comprehensive Legislative Plan
for pro rata fence modification (MWh for MWh)**

- a. TVA and TVPPA to work with Valley Congressional delegation to develop appropriate simplified legislation that provides for a pro rata fence modification that allows a ratable departure level of current and future TVA distributor load.
- b. Pro rata fence modification means TVA would have the ability to enter into wholesale power exchange arrangements with any wholesale entity, in addition to those identified in the 1959 amendment to the TVA Act, equivalent to the amount of energy (MWh) removed by a current or future noticing distributor from the TVA system, i.e., the amount to be served by a wholesale power supplier other than TVA. The amount of energy to be removed by a future noticing distributor would be limited by the available amount of energy determined by a cumulative ratable departure level. Current noticing distributors would be allowed to remove the entire amount of their load at the time of their contract term expiration.
- c. Ratable departure levels to be developed and described that allow future noticing distributors to implement partial requirements power supply arrangements. Annual ratable departure level to be adequate to allow reasonable and sufficient optionality for multiple distributors to evaluate and implement partial requirements options, yet limited to the extent that undue cost shifting among distributors is mitigated, and adverse ratings of TVA bonds are minimized. Ratable departure levels to be contractual rather than legislative.
- d. Formal TVPPA Board Resolution to actively support timely legislation for a pro rata fence modification
- e. Signed commitment by current noticing distributors to actively support timely legislation for a pro rata fence modification.
- f. Formal TVA Board Resolution supporting the elements described in the Comprehensive **Non-Legislative** Plan for Partial Requirements, Transmission Access, and Asset Ownership
- g. Current TVA/TVPPA/TVIC Consensus Title to be evaluated in context of agreements reached in Comprehensive Legislative and Non-Legislative Plans. Appropriate terms and conditions of Consensus Title to be addressed either legislatively or contractually. Appropriate Consensus Title disposition to be determined.